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No. 91-1436

IN THE
Supreme Court of the United States
OCTOBER TERM, 1991

NORMAN W. SWANSON, *et al.*,
Class A Petitioners,
and
CHARLES L. BERRY, *et al.*,
Class B Petitioners,
v.
THE STATE OF NORTH CAROLINA, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

PETITIONERS' REPLY TO BRIEF IN OPPOSITION

G. EUGENE BOYCE *
DONALD L. SMITH
JASPER L. CUMMINGS, JR.
WOMBLE, CARLYLE, SANDRIDGE & RICE
P.O. Box 831
Raleigh, North Carolina 27602
(919) 755-2100

CHARLES H. TAYLOR
4295 Shattalon Drive
Winston-Salem, North Carolina 27106
(919) 924-6064
Attorneys for Petitioners

* Counsel of Record

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STATEMENT OF THE CASE

Respondents have not misstated the facts underlying the instant case but have ignored facts necessary for this Court's proper determination of whether to grant a writ of certiorari to the Supreme Court of North Carolina. For example, Respondents purport to advise this Court that they have remedied the violation of Petitioners' rights by enacting a one-year tax credit for Class A Petitioners and a repeal of the unconstitutional tax for Class B Petitioners. (Opposition Brief, pp. 3-4.) Respondents do not mention, however, that these remedies were held to be inadequate as to Class A Petitioners and wholly ineffective as to Class B Petitioners. (Petition for Certiorari, hereinafter "Petition", App. G, pp. 61a-62a.) Petitioners set forth all necessary and pertinent facts in their Petition for Writ of Certiorari and now readopt and reiterate the facts as stated therein.

REPLY ARGUMENT

I. RESPONDENTS SEEK TO AVOID THIS COURT'S CONTROLLING DECISIONS BY IMPROPERLY RAISING ISSUES NOT BEFORE THIS COURT.

Respondents, in an apparent attempt to avoid this Court's decisions in *Davis v. Michigan Dept. of Treasury*, 489 U.S. 803 (1989), *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco of Florida*, 496 U.S. 18 (1990); *James B. Beam Distilling Company v. Georgia*, 501 U.S. ——, 111 S.Ct. 2439 (1991), and this Court's recent opinion in *Barker, et al. v. Kansas, et al.*, 91-611 (U.S. S.Ct., Slip Op., April 21, 1992), raise two issues not addressed by Petitioners in their Petition for Writ of Certiorari. Petitioners submit that neither issue is properly before this Court. In Section II of their Brief, Respondents argue that even if the *Davis* ruling applies to Class B Petitioners, significant differences exist between the duties of federal military personnel, Class B, and North Carolina National Guardsmen to justify the State's disparate treatment of Class B. (Brief in Opposition, p. 17, n.4.) Although Respondents made this argument for the first time in the Supreme Court of North Carolina, that

court did not address the issue. Respondents cannot raise an unlitigated issue to defeat the grant of a Writ of Certiorari. In addition, this Court's April 21, 1992 decision in *Barker, et al. v. Kansas, et al.*, 91-611 (Slip Op., April 21, 1992) resolves this issue as both the Kansas and North Carolina courts' treatment of federal personnel is inconsistent with this Court's decision in *Davis* and with decision of other state courts of last resort. *Barker*, Slip Op. at p. 3.

Respondents raise another issue not properly before this Court in Section III of the Brief in Opposition, by asserting that the Petition for Writ of Certiorari should be denied for the reason that Petitioners' claims for relief are barred by virtue of N.C. Gen. Stat. § 105-267 which statute requires a demand for refund within 30 days of payment of income taxes and denial of the demand or the lapse of 90 days before suit is instituted. The Supreme Court of North Carolina in its two 4-3 decisions did not address nor hold that N.C. Gen. Stat. § 105-267 bars this action even though these issues were thoroughly briefed and argued before that court. In any event, Petitioners made timely and effective class demands. (Petition, pp. 4, 5 and Apps. E and F.) Further, any requirement that Petitioners exhaust administrative remedies as a precondition to bringing a § 1983 action to protect federally guaranteed rights would violate this Court's ruling in *Felder v. Casey*, 487 U.S. 131 (1988). Petitioners' brief to the Supreme Court of North Carolina asserted the inapplicability and unconstitutionality of N.C. Gen. Stat. § 105-267 on thirteen different state and federal grounds. The only reference to the statute is in the dissent by Exum, C.J. (Petition App. A, p. 10a.) The constitutionality of this statute, facially and as applied is, however, the subject of another Petition for Writ of Certiorari pending before this Court in *Bailey, et al. v. The State of North Carolina, et al.*, No. 91-1434. In the case *sub judice*, Petitioners asserted in the Supreme Court of North Carolina the federal issues hereinafter discussed, all of which show that N.C. Gen. Stat. § 105-267 is not a bar to Petitioners' claims.

II. THE PETITION FOR CERTIORARI SHOULD BE GRANTED AS PETITIONERS' CLAIMS FOR RELIEF ARE NOT BARRED BY N.C. GEN. STAT. § 105-267.

A. It Has Been Judicially Determined Between The Parties On The Facts Of This Case That N.C. Gen. Stat. § 105-267 Does Not Provide An Adequate Remedy As Required By *McKesson*.

On Respondents' Motion to Dismiss Petitioners' 42 U.S.C. § 1983 action in the United States District Court, Eastern Division of North Carolina for declaratory and injunctive relief and for individual liability against the then Secretary of Revenue, Respondents asserted that N.C. Gen. Stat. § 105-267 controlled the issue of refunds and that this statute provided an adequate remedy. The assertion was relevant to Respondents' pleading the Tax Injunction Act, 28 U.S.C. § 1341, which denies federal court jurisdiction in state tax controversies unless the state remedy is not "plain, speedy and efficient." This Court in *Rosewell v. LaSalle Nat'l Bank*, 450 U.S. 503, 513 (1981) (citations omitted) equated a "plain, speedy and efficient" remedy with an "adequate" remedy. The United States District Court Judge rejected Respondents' arguments and expressly held N.C. Gen. Stat. § 105-267 to be an *inadequate* remedy for Respondents' unconstitutional taxation of Petitioners. (Petition App. G, p. 62a.) Accordingly, District Court Judge Howard's ruling is a final decision on the merits as to the inadequacy of the refund statute.[1]

Under the doctrines of collateral estoppel and *res judicata*, parties "are precluded from retrying fully litigated issues that were decided in any prior determination and were necessary to the prior determination." *King v. Grindstaff*, 284 N.C. 348, 356, 200 S.E.2d 799, 805 (1973) (federal court judgment binding on parties in state court for *res judicata* and collateral estoppel purposes; parties

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[1] Only Judge Howard's decision on qualified immunity was reversed. 937 F.2d 965 (4th Cir. 1991), *cert. denied*, 116 L.Ed.2d 777 (13 January 1992).

precluded from retrying fully litigated issues that were decided in any prior determination and were necessary to the prior determination).

While collateral estoppel and *res judicata* have technical distinctions, both doctrines prohibit Respondents from relitigating the issue of the adequacy of the remedy provided by N.C. Gen. Stat. § 105-267. Moreover, both doctrines apply in tax litigation and may operate as a bar against taxing authorities. *See Russell v. C.I.R.*, 678 F.2d 782 (9th Cir. 1982); *U.S. v. Nez Perce County, Idaho*, 553 F. Supp. 187 (D. Idaho 1982); *State Bd. of Equalization v. Superior Court*, 703 P.2d 1131 (Cal. 1985); *Hanson v. Oregon Dept. of Revenue*, 653 P.2d 964 (Or. 1982). Thus, Respondents may not relitigate the adequacy of the remedy provided by N.C. Gen. Stat. § 105-267.[2]

B. Application Of N.C. Gen. Stat. § 105-267 Is Unconstitutional On The Facts Of This Case.

At issue before the Supreme Court of North Carolina (but not addressed by that court) was the manner in which the State sought to invoke the 30-day demand requirement of N.C. Gen. Stat. § 105-267, and whether, *under the facts of this case*, Respondents' actions satisfy the commands of the Due Process Clause. This Court has recognized that the constitutionality of administrative demand requirements of a taxing authority must be determined "under all the circumstances" of the case. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 314, (1950). Therefore, the undisputed facts of this case as

[2] It should also be noted that all necessary inferences from a judgment or decree will be given preclusive effect for purposes of collateral estoppel and *res judicata*. *See Metals Disintegrating Co. v. Reynolds Metals Co.*, 98 F. Supp. 201 (D. Del. 1951); *Joseph Rubin & Sons v. Waverly Const. Co.*, 97 N.Y.S. 2d 753 (N.Y. Sup. 1950). Accordingly, if anything can be inferred from Judge Howard's decision, it is that N.C. Gen. Stat. § 105-267 does not, under the facts of this case, provide an adequate remedy as required by *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco of Florida*, 496 U.S. 18 (1990).

found by Judge Howard (Petition, App. G), concerning the timing of Respondents' drastic change of departmental policy relating to refunds, are relevant.

Respondents knowingly and in bad faith singled out Petitioners in arbitrarily applying a 30-day rule which they were unable to effectively administer and which was contrary to pre-*Davis* practice and official publications. (Petition, App. G, pp. 59a-61a.) Respondents seek here to plead the statute as a bar to this Court's granting certiorari in a case in which Respondents collected taxes in violation of federal law. The use of the statute to defeat federal claims violates supremacy clause requirements, is legally inadequate and does great harm to a tax system dependent upon notions of fair play, accountability and responsiveness.

First: Respondents' abrupt change of policy in their post-*Davis* explanation of the governing remedy is analogous to retroactively shortening a statute of limitations. Statutes of limitations may be shortened only if done while the time is still running, *and* so that a reasonable time still remains for commencement of an action before the bar takes effect. *Ochoa v. Hernandez y Morales*, 230 U.S. 139 (1913). Due process of law requires that Petitioners be given adequate notice of the abbreviated remedy. They were not. (Petition, App. G., p. 60a.) *See also*, *Brinkerhoff-Faris Trust & Savings Co. v. Hill*, 281 U.S. 673, 682 (1930). ("Whether acting through its judiciary or its legislature, a state may not deprive a person of all existing remedies for the enforcement of a right, which the state has no power to destroy, unless there is, or was, afforded . . . some real opportunity to protect it.") *Second*: thirty days is too short a time period as the average taxpayer could not reasonably be expected to make a demand under Respondents' post-*Davis* refund policy. *Cf.*, *Chambers v. Omaha Public School Dist.*, 536 F.2d 222, 229 (8th Cir. 1976) (indicating that a six-month statute of limitations is too short to protect federal rights). *Third*: because Respondents simply looked to the date on which the return was signed, rather than when

it was actually filed, for determining when the 30-day period began to run (for the purpose of judging whether a demand was timely) they operated in a random fashion and effectively denied thousands of retiree taxpayers due process of law. (Petition, App. G., p. 60a.) *Fourth*: Respondents' eleventh-hour change of the State's refund policy by invoking the 30-day demand requirement failed to comport with due process because Respondents failed to give federal retirees "a clear and certain remedy" or the opportunity to be heard "in a meaningful time and in a meaningful manner." *McKesson*, 110 S.Ct. at 2238. Respondents utterly failed to give Petitioners a "fair opportunity to challenge the accuracy and legal validity of their tax obligation." *McKesson*, 110 S.Ct. at 2251. Accordingly, the actions of Respondents violated Petitioners' rights to due process, and the demand requirement of N.C. Gen. Stat. § 105-267 cannot be used to bar claims for refunds.

III. N.C. GEN. STAT § 105-267 IS UNCONSTITUTIONAL ON FOUR INDEPENDENT FEDERAL GROUNDS.

As noted in the recent case of *47th Street Photo, Inc. v. Powers*, 100 N.C. App. 746, 748, 398 S.E.2d 52 (1990), *app. dism., rev. denied*, 329 N.C. 268, 407 S.E.2d 835 (1992) there is an issue of "whether § 105-267 (a 'post-deprivation procedure') provides a sufficiently 'clear and certain remedy' to satisfy federal due process principles." While relatively short statutes of limitations may be permissible, N.C. Gen. Stat. § 105-267 results in an unconstitutional deprivation of due process and equal protection of the laws and a violation of the Supremacy Clause for a reason other than the brevity of its limitation period. It subjects tax refund claims based on federal constitutional grounds to a shorter statute of limitations than the refund claims based on mere error. N.C. Gen. Stat. § 105-266.1 (1989). A statute of limitations is unconstitutional if it improperly discriminates between similarly situated plaintiffs. *See Pickett v. Brown*, 462 U.S. 1 (1983) (shorter limitations period afforded illegitimate children than to

legitimate children for paternal support actions held unconstitutional).

The equal protection clause of the Fourteenth Amendment protects taxpayers from discriminatory treatment by the State in subjecting them to taxes not imposed on others. *Hillsborough v. Cromwell*, 326 U.S. 620 (1946). Respondents' distinction between aggrieved taxpayers who seek refunds exacerbates the initial discriminatory practice of imposing taxes on Petitioners that were not imposed on others. Accordingly, the further distinction independently violates equal protection.

The State's purported refund scheme is unconstitutional as a burden on a federal right. Respondents' position may be stated as follows: if the State overtaxes because of miscalculation, a refund may be obtained within three years, N.C. Gen. Stat. § 105-266.1; if the State taxes in violation of the United States Constitution, a demand for refund must be made within 30 days or all right to refund is lost. N.C. Gen. Stat. § 105-267. In *Republic Pictures Corporation v. Kappler*, 151 F.2d 543 (8th Cir. 1945), *aff'd per curiam*, 327 U.S. 757 (1946), the court held that a state could not discriminate against federal rights by applying a shorter statute of limitations than that applied to similar rights under state law. The rule is violated by Respondents singling out Petitioners and arbitrarily applying N.C. Gen. Stat. § 105-267 to defeat federal constitutional claims while permitting the three year remedy of N.C. Gen. Stat. § 105-266.1 for claims based on other grounds.

Respondents' classifications are not *rationally* related to a *legitimate* governmental purpose. *Clark v. Jeter*, 486 U.S. 456 (1988); *G.D. Searle & Co. v. Cohn*, 455 U.S. 404 (1982). A recent New York case is illustrative. In ruling that the disparate treatment violated equal protection, the court reasoned that:

> The municipal respondents . . . provide no basis, and we can think of none, upon which to conclude that a rational relationship exists between the Legislature's

> laudable goal [of preserving the economic well-being of the local jurisdictions] and the deprivation of LILCO's statutory right to seek judicial review of the tax assessments . . . while other similarly situated taxpayers continue to enjoy such a right. The integrity of any system of taxation . . . rests upon the premise that similarly situated taxpayers pay the same share of the tax burden.

Long Island Lighting Co. v. Brookhaven, 154 A.D.2d 188, 552 N.Y.S.2d 336, 340 (1990). *See also, Gosnell Dev. Corp. v. Dept. of Revenue*, 154 Ariz. 539, 744 P.2d 451 (1987) (prospective rather than retrospective application of taxpayer-favorable ruling impermissibly discriminates against taxpayer in favor of its similarly situated competitors). While "sound fiscal planning" and "lessen[ing] the risk of loss" may be legitimate governmental purposes, "*the State's interest in financial stability does* not *justify a refusal to provide relief.*" *McKesson*, 110 S.Ct. at 2257.[3]

Refund distinctions imposed by Respondents are not only financially unjustified, but are also irrational in light of the relative apportionment of responsibility in discovering the various types of error which can lead to tax overpayment. It is generally accepted as rational the application of a shorter statute of limitations to potential claimants who possess special knowledge necessary

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[3] Likewise, in granting refunds to federal retirees in *Hackman v. Dir. of Revenue*, 771 S.W.2d 77 (Mo. 1989), *cert. denied*, 493 U.S. 1019 (1990), the Missouri Supreme Court, sitting *en banc*, stated: We are not, of course, deaf to the public pronouncement that

> We are not, of course, deaf to the public pronouncements that the precedent established by this case bears a potential $150,000,000+ cost for the State. Nevertheless, whether the State has appropriated the funds necessary is not relevant to our consideration of the merits of appellants' claims in this case. The role of the judicial branch under these circumstances is "to adjudicate whether the State is obligated . . . It remains for the General Assembly to appropriate the money if it be determined that the State is so obligated."

771 S.W.2d at 82.

to discover a claim or whose responsibility it logically would be to investigate whether a claim exists. *See, United States v. Kubrick*, 444 U.S. 111, 120-21 (1979) (discussing propriety of statutes of limitation in medical malpractice context). That clearly is not the case here.

When the potential claimant, as the taxpayers here, lacks special knowledge, due process requires a longer statute of limitations be afforded so that the taxpayer will have adequate time within which to assert a claim. Such a longer limitations period is not unfair to the Respondents because they have superior knowledge and expertise.[4]

Under N.C. Gen. Stat. § 105-264, taxpayers are entitled to rely on the Secretary's published interpretations. Such misinformation and inherent unfairness in Respondents' reliance on N.C. Gen. Stat. § 105-267 irrationally misplaces responsibility and violates equal protection and due process of law.

CONCLUSION

Respondents seek to have this Court deny the Petition for Writ of Certiorari on grounds not relied on or addressed by the Supreme Court of North Carolina. If this Court should deny the Writ for these reasons, Petitioners would not only be denied a meaningful remedy

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[4] As concluded by Judge Howard, the Secretary has "the statutory responsibility to regulate, monitor, advise, and *act upon* problems in administering the tax code." (Petition, App. G. p. 64a.) (Emphasis added.) The Secretary is specifically charged by statute to make thorough study and reports on income taxation laws, including comparison between state and federal taxation, and she is specifically charged with reporting regularly to the General Assembly on problems and making recommendations. N.C. Gen. Stat. §§ 143B-218, 143B-219, 147-88, 105-257 and 105-453. Thus, the Secretary is in the best position to publish accurate and reliable interpretation and guidance regarding income tax laws, including applicable refund statutes.

for the unconstitutional taxation but would be denied *any* remedy whatsoever. This Court should grant certiorari for the simple reason that the Supreme Court of North Carolina erroneously applied *Chevron Oil Company v. Huson*, 404 U.S. 97 (1971) to the facts of this case in the face of pre-existing North Carolina law that made the State's constitutional violations apparent under 4 U.S.C. § 111 and the doctrine of intergovernmental tax immunity. (Petition, pp. 10, 11, n.3.) The court's misapplication of *Chevron* effectively violated Petitioners' guaranteed federal rights and was a thinly veiled attempt to protect the state's fisc and justify the state's arbitrary treatment and callous disregard of Petitioners' valid class refund claims. The Respondents' claims that they acted in good faith and provided an adequate remedy to Class A and Class B Petitioners are merely a subterfuge to hide the Supreme Court of North Carolina's egregious error. This Court should, therefore, grant a Writ of Certiorari and reverse that court's judgment.

Respectfully submitted,

G. EUGENE BOYCE *
DONALD L. SMITH
JASPER L. CUMMINGS, JR.
WOMBLE, CARLYLE, SANDRIDGE & RICE
P.O. Box 831
Raleigh, North Carolina 27602
(919) 755-2100

CHARLES H. TAYLOR
4295 Shattalon Drive
Winston-Salem, North Carolina 27106
(919) 924-6064
Attorneys for Petitioners

May 6, 1992

* Counsel of Record